
TAX REFORM CONCLUSION:

If we accept the preceding proposal on tax reform we will end up with a system which imposes **NO** personal income taxes and revises the business income tax to refocus its based on the rate of return on capital (yield). Real estate becomes subject to a 2% retail sales tax and everyone will be subject to a 10% retail sales tax. **To help the poor, UNPREPARED food, housing rents and health care should be exempt from the sales tax.** Lobbying goals will be much more difficult to accomplish since any tax exemption will be restricted to an industry group or sector rather than on an individual basis. The public will become immediately aware of any such lobbying efforts since such tax exemptions will noticeably stand out in a crowded room. The benefits to this plan are not only those as previously mentioned with respect to broadening the tax base via the underground economy, but also an elimination of the countless other incidental forms of regulation and taxes. Excise taxes will remain in effect, but luxury taxes, inheritance, capital gains and worldwide income will no longer be necessary. Such a proposal will return the nation to a form of taxation that is much closer in design to that originally intended by our Founding Fathers. It was through their experience and wisdom that the Constitution intentionally prohibited direct taxation of income due to its infringement upon personal liberties.

Until 1913, the revenue of the nation was always produced through excise and indirect methods of taxation. *(The shift from an indirect method of revenue collection to a direct system of income taxation has led to the fundamental violation of the Constitution's intended principles with regard to the burden of proof which then necessitated the 16th Amendment to the Constitution.)* There is perhaps no clearer illustration than the fact that a murderer remains innocent until proven guilty but the IRS code declares a citizen to be guilty first leaving him with the his obligation to prove his own innocence while interest and penalties continue to multiply. This approach has been adopted because government argues that it does not have the resources to audit every individual. Simply, this approach is in total contradiction to everything our fathers fought and died for since the birth of this nation. We also argue that when other nations use this approach we call it a **VIOLATION OF THEIR CIVIL RIGHTS**. The United States needs to practice what it preaches.

STRUCTURAL REFORMS

The following represent suggestions for structural reforms that should be implemented in order to redirect and improve the function of government itself thereby insuring our long-term viability as a nation.

I. THE DANGERS OF A BALANCED BUDGET AMENDMENT

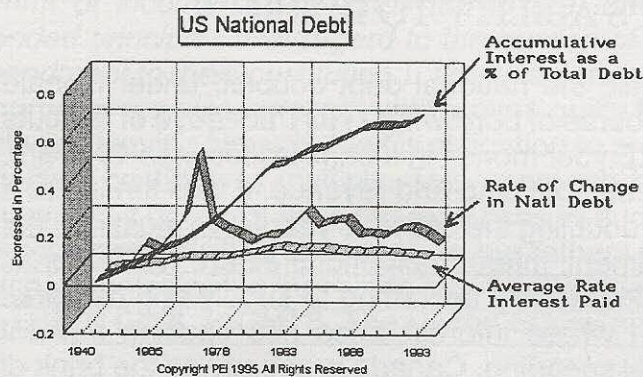
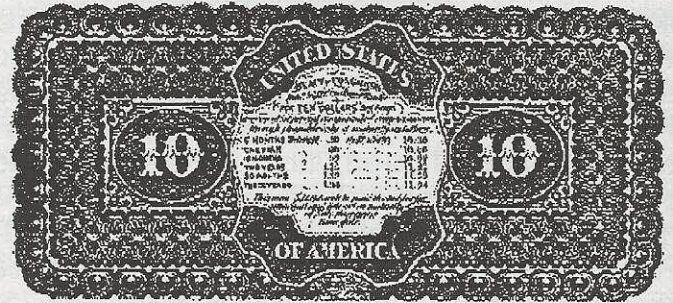
What is often mistaken is the fact that a Balanced Budget Amendment will solve all the problems of mankind. Such an Amendment will **ONLY** mandate a balanced budget - **NOT** insure reduced taxation or spending. Taxes could actually be raised under such an Amendment in a mandated form under Constitutional Law. The real imperative must be a **strict limitation on government spending as a percent of GDP**. Furthermore, the current situation that has produced the silent encroachment of tax regulation, would **STILL** have taken place given a **SUPER MAJORITY** rule. Such concentration of power within one party **DOES** historically take place over time. The income tax was originally passed with the solemn promise that it would be lifted once World War I was over. Instead, the income tax remained in effect following WWI and in fact even broadened to include most Americans following WWII. The key to prevent such a silent encroachment in the future is a **CONSTITUTIONAL AMENDMENT** mandating that any tax increase will automatically expire after 4 years and will require a national referendum for its renewal. Combining this protection with a strict limitation of the size of government as a percent of **GDP** is the answer to the future. Of course the formula to calculate **GDP** **MUST** be incorporated within such an Amendment or else this too can easily be manipulated to allow for higher taxes and spending in the future.

II. RESTRICTING GOVERNMENT'S ABILITY TO BORROW

What we must realize is the fact that while the national debt doubled under Ronald Reagan's 8 years, it did so out of a natural course of borrowing - **NOT** because of tax cuts or economic philosophy. At 8%, you **DOUBLE** your money in a bank in less than 10 years. Reagan actually balanced the budget between spending and revenue. It was the interest expenditures that equaled \$1 trillion thereby doubling the debt in 8 years. We must respect that even under a Balanced Budget Amendment, interest expenditures are **NOT** subject to decree but remain a function of free market activity according to supply and demand. We could still find ourselves in a position where interest rates rise causing interest expenditures to grow as a percentage of total spending. Canada is already on the brink of a default since its interest expenditures are consuming over 42% of every dollar the government spends. Therefore, we must broaden our understanding of this process and impose strict limitations upon government's ability to borrow. Deficit spending must be prohibited unless in time of war or recession. The old argument that government spending stimulates the economy works only if such spending moves directly into the domestic economy. Today, however, much of that spending moves offshore and into the hands of foreign holders of our national debt. This type of spending accomplishes **NOTHING** from a domestic stimulus perspective while contributing to the overall decline in national wealth.

III. IS IT LESS INFLATIONARY FOR GOVERNMENT TO BORROW

We must also realize that borrowing to fund a deficit rather than monetizing is **NOT** necessarily less inflationary. In fact, it has been the interest expenditures that are now forcing the creation of money in the form of bonds, notes and bills. While government may restrict some securities from being placed as collateral in an attempt to differentiate between securities versus cash, such limitations are **NOT** applicable to non-domestic holders of debt. Furthermore, banks are not prohibited from lending on such securities when they are grouped as assets for a loan that carries a personal guarantee. Through this method of borrowing, the assets are not actually pledged as collateral thereby converting such securities to cash. A domestic holder of debt may also place such securities with a non-US bank where these restrictions do not apply. Government securities may also be used as margin in financial transactions. Since 33% of the national debt is funded 1 year or less, the bulk of this debt has merely added to the money supply removing any advantage of creating less inflation. In any event, it is impossible for government to issue bonds, notes or bills that are not a form of cash that does not expand the money supply.



Illustrated above, is a **\$10 Treasury Note** from the Civil War period. Due to the paper money hyperinflation of the Revolution, the federal government issued only gold, silver and copper coinage between 1792 and 1860. When paper currency was reintroduced, it was in effect a circulating bond that paid interest according to the schedule printed on the reverse. It is likely that the issuance of securities actually results in raising the core rate

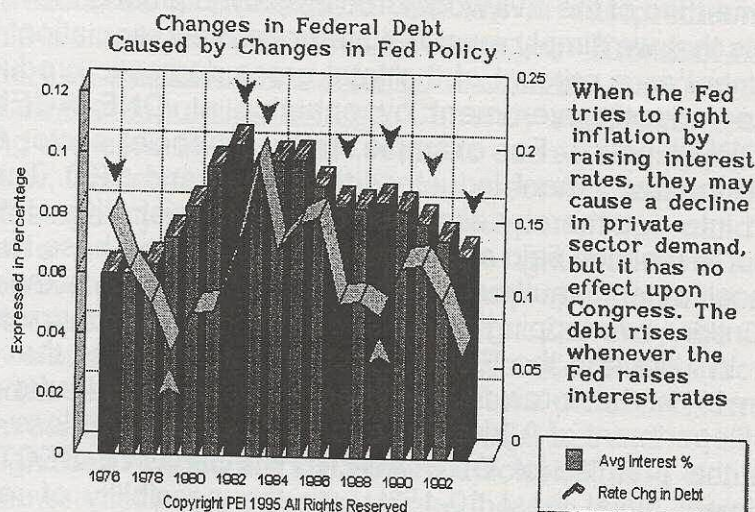
of inflation by increasing government expenditure to cover the perpetual debt that has developed. Borrowing might be less inflationary provided such debt is **ONLY** temporary. But when a national debt becomes a fixed part of life, the less inflationary influence no longer applies and in the end, creates greater levels of inflation long-term. From an accumulative perspective, the total interest expenditures since 1940 have been \$3.0019 trillion as of 1993, representing 68.9% of the total national debt \$4.3512 trillion.

IV. FEDERAL RESERVE'S INABILITY TO CONTROL INFLATION DUE TO CONGRESSIONAL INTERFERENCE

The traditional role of the Federal Reserve has evolved as defender against inflation. The problem that the Fed now faces is its inability to perform such a role while lacking control over Congressional spending habits. When the central banking system was established in 1913 following the financial Panic of 1907, its charter expressly provided for managing our national money supply and cash flows. It was determined that the Panic of 1907 took place due to a cash flow problem caused by massive insurance claims paid from the East to the West in the wake of the famous 1906 San Francisco earthquake.

Therefore, 12 branches of the Fed were set up with each maintaining a totally independent discount rate as its tool to attract or deflect regional capital flows. In 1927, the powers of the branches were consolidated in an effort to perform the same task, but internationally. In 1927, the Fed lowered US interest rates trying to deflect capital back to Europe where serious shortages were arising. That misguided action backfired and the capital flows intensified pouring into the US on rumors of European government defaults. This led to the US share market doubling in price and the Fed responding by reversing course to raise interest rates from 3% to 6% going into the peak of 1929 activity. The Great Depression was more a result of massive government defaults on debt than private sector stock speculation. In fact, the German bond default alone was \$10 billion compared to \$6 billion at the peak in broker loans during 1929. All of Europe permanently defaulted on its debt, with the exception of Britain and Switzerland. Added to these defaults were China, Russia and most of South America. More than 16 times the losses in the US share market took place in government bond markets wiping out capital formation and savings.

Since the Great Depression, the Fed has been trying to control inflation by raising or lowering interest rates in hopes of affecting private sector demand. The problem we now face is quite simple. In 1929, the US national debt stood at less than \$30 billion. Government was a very small portion of that demand for capital in the marketplace. Today, government is the single largest debtor within society. When the Fed raises interest rates to reduce the demand for capital, it might have an effect within the private sector, but it has NO effect whatsoever upon Congress. Unless Congress is forced to respond in an appropriate manner as any homeowner, then there is little hope of solving the problems of long-term fiscal irresponsibility. Spending must be linked to GDP- **NOT** political agendas.



Due to changes in Treasury funding strategies, the lag time between rate hikes at the Fed and changes in interest expenditures has been declining. During the late 1970s, there was a 3 year gap between the effects of interest rates and changes in the debt. By early 1980, the lag time declined to 2 years and in the 1990s it is 1 year

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V. ONE AGENCY - ONE REGULATION AUTHORITY A STANDARD OPERATIONAL REFORM SAVING BILLIONS

A massive government consolidation effort **MUST** be undertaken. We simply cannot afford one-third of the civil work force employed among the ranks of the public sector. This suggests that we simply must reduce not merely regulation, but also the size and cost of government as a percent of the total gross domestic product. We must launch a major effort to reduce government by enacting a **ONE AGENCY - ONE REGULATING AUTHORITY** policy. For example, in the financial sector there are two agencies that regulate the investment industry - the CFTC and SEC. These two agencies should be merged into one thereby eliminating two administrative staffs, accounting and management not to mention field agents. A consolidation of these two agencies, which constantly battle each other for authority, would save at least 25% of the current combined cost. There are countless overlapping examples between the Department of Agriculture and National Parks, Wildlife and the EPA, etc. One would assume that the famous Smoky the Bear program to combat forest fires belongs to the National Parks - wrong this a program funded by the Department of Agriculture. The list is simply endless. A massive consolidation that follows the premise of **ONE AGENCY FOR ONE SECTOR** will reduce the cost of government by at least 10-15% with the possibility of reaching savings as great as 20%-25%.

- a). In addition, a major review of regulation is required. The EPA has caused serious damage to American business as well as homeowners through the enforcement of Wetlands. This regulation, while intended to protect natural wetlands from development, is enforced based on a vague definition that is applied to drainage ditches along the side of a road or to a man made environment. There are no safeguards that limit such enforcement to "natural" habitat - resulting in numerous cases of driveways and even backyards within an existing development being classified as "wetlands." Such vague regulations have been imposing fines that are far too excessive in violation of the Constitutional guarantee that prohibits government from imposing "excessive" fines or fees upon the citizens of our nation.
- b). Competing regulation between the CFTC and the SEC has resulted in numerous US fund managers moving offshore and refusing to deal with Americans due to contradictory regulations. While this is a vital industry in which America is the leader in the world, these two agencies cannot agree upon basic rules forcing this industry to leave in search of more reasonable regulatory environments. Only the US has two agencies while all other nations manage to regulate the financial industry with one body of code and one authority. All sectors of business must be granted this relief.

VI. REQUIRE AGENCIES TO BE ACCOUNTABLE UNDER THE INTERPRETATIONS AND REGULATIONS ISSUED

In addition to legal reform, a MAJOR EFFORT should be considered where a sharp reduction in the number of court cases and over regulation can be handled. The one **NEW** government agency that **MUST** be created is a separate review panel of judges that will determine the Constitutionality and legislative intent of any new regulation or interpretation on the part of any agency before such regulation or interpretation is enacted or enforced. Currently, a private citizen cannot challenge a new law until that law inflicts **HARM** on an

individual. Once a **HARM** has been inflicted, it becomes that individual's right to appeal any government action through the various layers of legal courts and perhaps as far as the Supreme Court itself - provided he has the legal resources to do so. If the individual does **NOT** have the financial resources to challenge a new law or interpretation, the government wins by default. This is simply immoral within a free society. Therefore, a new agency must be established where all agencies are compelled to seek the approval of that panel BEFORE inflicting harm on the population at large. Currently an agency tests its theory of interpretation by finding someone in the private sector to use as a ginny pig. This is how the agency establishes law. It is totally unreasonable to expect this cost to be born by the private sector. Instead, the agency must go before a review panel that would then make the determination. A citizen or an agency would then have the right to take this review panel to court if it so desires. However, this new agency will act as a proper buffer between government and the private sector against the abuse of agency power. Currently, the CFTC is waging a battle to force all newsletter writers in the nation to register despite the fact that the Supreme Court already ruled in 1985 against the SEC for the same practice. However, the CFTC takes the position that the Supreme Court ruled on the SEC act and not directly the CFTC's authority even though their actions are still unconstitutional. This is clearly an abuse of power since unless a newsletter has the capital to take them to court, no relief is possible and the CFTC can continue its violation of our right to freedom of speech. Such a review panel will also help in the nightmare that has arisen over various regulations that in effect result in an unlawful "taking" or confiscation of private assets without fair compensation. This will reduce the number of cases that are causing a backlog in the courts and thereby reduce the mounting pressure to establish more courts at the expense of the taxpayer. This new agency would have final authority over **ALL** agencies. Any new REGULATION or INTERPRETATION that goes into effect would therefore already be clarified as to its Constitutionality saving billions and mountains of red tape.

VII. MAKE IT A FEDERAL CRIME FOR ANYONE WHO INTENTIONALLY WASTES PUBLIC FUNDS OR WHO INTENTIONALLY REDIRECTS PUBLIC FUNDS FOR OTHER THAN INTENDED PURPOSES.

The typical budget process, both federal as well as state and local, works under the premise that spending for the next fiscal year will be determined by the expenditures of the previous fiscal year. This policy promotes corruption within governmental departments at all levels. It is a rare department that actually spends every last dime of its budget without finding last minute expenditures. Consequently, departments usually go on a spending binge trying to make sure that they have spent everything they were allotted in an effort to guarantee the same budget or more for the upcoming fiscal year. This practice leads to major waste of public funds on an intentional basis, which constitutes legal fraud. This practice is so widespread, that every level of government is involved. In one case in New Jersey, a department involving road engineering spent unused funds on a huge shipment of computers and then warehoused them while the department of education argued for an increase in their budget that would enable them to buy computers.

It should be declared FELONY for any public servant to intentionally divert public funds from their original intended purpose or to intentionally spend public funds for budgetary purposes. Perhaps the most notorious example of this type of fraud also stems from New Jersey involving the former Governor James Florio. Florio actually sold a stretch

of road for several hundreds of millions of dollars to the New Jersey Turnpike Authority, which then floated a bond issue in order to pay for this non-toll road. The maneuver by Florio was created because the state has a Balanced Budget mandate, which prevented the state itself from issuing such bonds. The funds were then added to the budget of the state to finance other unrelated social spending circumventing its Constitution. **This type of fraud illustrates again how a Balanced Budget Amendment will NOT prevent government waste unless we make intentional circumvention illegal!**

The former New York Governor Mario Cuomo similarly raided state employee pension funds in order to finance state spending projects. This funding was so significant, that the state pension fund could be threatened since it will now require an investment return in excess of 10% annually to cover the long-term liabilities. No private company would be allowed to use the funds of its employees to pay for company projects and again this type of mismanagement would be subject to criminal prosecution if it took place corporately.

These types of abuse of public funds constitute a fraud that would be punishable under any criminal law in the private sector. **Unless government officials are held to the same high standards as anyone in the private sector, the corruption within government cannot be changed.** This type of behavior offers a serious danger to the financial stability of the nation. It also threatens our very future by promoting a crisis **NOT** unlike that of the S&L industry where ultimately the cost must be born by the taxpayer.

VIII. RESTORE LEGISLATIVE INTEGRITY: GERMANE DEBATE AND AMENDMENT

To eliminate the pork-barrel politics that has propelled the budget crisis, NO bill in the House or Senate should be amended with any proposed spending, regulation or state mandate that is NOT directly related to the nature of the bill in question. In other words, no grants to favorite universities and no midnight basketball funding labeled as fighting crime! Any crazy study to watch the flow rate of ketchup would have to be proposed as a stand-alone bill and the author would have to face the consequences for doing so.

IX. GOVERNMENT JOBS SHOULD BE USED AS SAFTEYNET

We must realize that many government employees are in fact public servants that contribute nothing to the overall creation of national wealth. This is not to say that government employees do not contribute a vital "service" to society or that they are completely unnecessary. But when we view government services from an economic perspective there is no difference between this group and hiring a maid. Therefore, if too many people end up in the employ of government, taxes must rise in order to pay for this service that cannot be exported as a tangible commodity. Adding this group to the unemployed and welfare segments of society and we begin to approach 50% of the civil work force numbers thereby necessitating a tax rate of at least 50%. Government jobs where clerical or unprofessional skills are required should act as a safteynet for society. In other words, if someone loses their job, they should work for government fulfilling some service task in return for compensation. At such time when the individual can find work back in the private sector, he would leave in order to gain greater salary. This type of program might be controversial, but it is necessary to provide compensation while costing the taxpayer an absolute minimum since he must currently pay for both the government employee and the unemployed or welfare citizen.

EXAMPLES OF PROGRAM REFORM

PRIVATIZING FOOD STAMP REFORM:

Food stamps have become a quasi form of currency traded openly on the black market at rates between 60 and 80 cents on the dollar. Drug addicts often sell their food stamps for cash and then proceed to buy their illegal goods. Retailers are able to buy such stamps at a discount and redeem them with the government without fear of prosecution. The reason why this trade takes place is that there are far too many retailers and not enough government agents to audit.

SOLUTION: The food stamp program can be easily fixed **NOT** by issuing magnetic cards that can still be fraudulently used, but by privatizing the system. Instead of food stamps being issued in dollar amounts, which creates conflict over how much money is required to feed a family, benefits should be distributed in specific coupons redeemable for tangible products. The total benefit will be provided in a much more efficient manner such as quantities of bread, milk, eggs and cans of soup etc. Producers will compete by submitting bids to the government that will enable these coupons to be redeemed for their particular product. The advantage to the private sector will be the program's ability to deliver market share. The advantage to the government will be a drastic reduction in the cost to provide a food stamp service to the public. Contract bids may **NOT** pay more than the going wholesale rate for such products in that particular region. The recipient will receive the coupons based upon consumption requirements. The retailer will then provide the product specified by the coupon. In turn, the retailer will redeem the coupons for a specific product with the distributor or producer. He will receive a check for his normal markup and replacement product. The producer will then collect the coupons and submit them to the government for prompt payment on a monthly/and or weekly basis according to the agreed upon contract bid price.

Since the number of producers are but a small fraction of the total number of retail grocers, the amount of effort required to do a full and fair audit is greatly reduced. This type of system is **MANAGEABLE** and **ACCOUNTABLE** as compared to the current system.

BENEFITS:

- 1) Eliminate the black market since retailers can only redeem the same number of coupons that match the number or products purchased from the distributor/producer.
- 2) Recipients will receive a specified food supplement for their family group that will insure nutrition rather than the current program where food stamps can be used for cigarettes or beer. Parents who now cash in their food stamps and feed their children with the bare minimum, will be **UNABLE** to resell their coupons on the black market thus insuring that the children will in fact receive the proper food.
- 3) The fraud eliminated by this approach will provide significant savings in the effort to balance the budget. In addition, the lower cost of this program will also enable an

extension of the program in a way that will provide partial benefits to those willing to move off of welfare and into the job market while retaining at least a partial benefit during the transition period.

MEDICARE REFORM

The medicare program is another area where costs are exploding and government lacks the ability to verify that they are being properly billed for service actually provided. In our investigation, the most common practice that leads to fraud has been the billing for services never provided. Within our own office, out of a group of 10 people interviewed, 3 reported being billed for visits or tests never performed within their families. In one case, medicare was billed for care that was never provided. When medicare was informed of this fraud, they simply replied that they did not have the time to investigate every claim. In another case, a patient's name was used as having made 3 visits per week that never took place. In this case, the doctor was confronted directly. His reply was that they typically billed people who would be covered in order to provide service for those who could not pay or had no insurance.

There is **ABSOLUTELY NO WAY** government can honestly verify any claim submitted for health-care service. What we need to do is use Ronald Reagan's approach to the Russians - trust, but verify. This can be accomplished by issuing a type of credit card that then must be used in order to submit any claim to the government. Each test performed **MUST** display an imprint of this card on the form and signed by the patient. This will accomplish a major step in stemming fraud. At least we will know that a test was performed and to insure patient help in policing against fraud, we should provide for a 5% rebate to all member programs if they have used less than some fixed amount such as \$1,000 or some number that proves to be fiscally responsible.

SOCIAL SECURITY INVESTMENT REFORM

Currently the Social Security fund is "technically" off-budget. However, it is still calculated back in the numbers to reduce the appearance of the deficit. The **ONLY** way we can instill honest off-budget approach is to legally change the management structure of this fund. At this time, the SS fund is **NOT** professionally managed in any way and acts as nothing more than a slush fund for the Treasury. Government deficits can rise knowing that they have the SS fund sitting there with cash that can be forced to buy their bonds, notes or bills. What we must institute is a new independent system of management. The postal savings system of Japan contracts out all management of its funds - the largest such public trust fund in the world. Various banks, insurance companies and fund managers line up to do the actual management. Some stipulations can be attached such as not more than 25% of total assets may be invested in equities etc. The important aspect is that we will insure that the numbers from SS will no longer be put into the general pot as a diversionary tactic to make the deficit appear to be lower than it is. This will also prevent Congress from raising the SS withholding to avoid pledges against raising taxes. This is why the SS rate has risen by more than 30% over the past several years since any increase in the rate of withholding will ultimately reduce the deficit despite "technically" being off budget.